FISCAL NOTE

Bill #:	SB0048	**Title:**	Eliminate the Class 8 Trigger and Increase the Class 8 Threshold to $20,000
Primary Sponsor:	Harrington, D.	**Status:**	Second Reading

Sponsor signature Date | David Ewer, Budget Director Date

Fiscal Summary

	FY 2006 Difference	FY 2007 Difference
Expenditures:		
General Fund	$18,720	$201,720
Revenue:		
General Fund	($171,716)	($456,864)
State Special Revenue	($11,610)	($30,889)
Net Impact on General Fund Balance:	($190,439)	($658,584)

☒	Significant Local Gov. Impact	☐	Technical Concerns
☒	Included in the Executive Budget	☒	Significant Long-Term Impacts
☐	Dedicated Revenue Form Attached	☒	Needs to be included in HB 2

ASSUMPTIONS:

Department of Revenue

1) This bill removes the "trigger" that would result in the reduction in the tax rate for class 8, business equipment property from 3 percent to 0 percent over a three-year period. In effect, the bill provides that class 8 property will remain taxed at 3 percent unless future legislatures change that rate. The bill also increases the threshold amount of class 8 property that an entity may own and be exempt from property taxation from $5,000 of market value to $20,000.
2) This bill is effective upon passage and approval; therefore, the class 8 trigger is repealed upon passage and approval of this bill. The proposal applies to property tax years beginning after December 31, 2005, so the increase in the exemption threshold allowed for class 8 property will take effect in tax year 2006.
3) Most property taxes are paid in November and May of the fiscal year following assessment. However, under the provisions of 15-16-119, MCA, owners of personal property that is not-liened to real property pay property taxes 30-days after assessments are mailed. This means that instead of paying taxes in November and May of the following fiscal year, they will pay sometime before April in the current fiscal year. Therefore there are some FY 2006 impacts associated with the bill.

INCREASE CLASS 8 EXEMPTION THRESHOLD LEVEL FROM $5,000 TO $20,000

4) Because of the applicability date, the increase to the class 8 exemption threshold under SB 284 has a partial year impact on property tax revenue in FY 2006, and a full year impact in FY 2007. The estimated FY 2006 and FY 2007 reductions in property tax revenue from the increased exemption threshold level are shown in Table 1.

Table 1
Impact of Increasing the Class 8 Exemtion to $20,000
On Property Tax Collections

	FY 2006	FY 2007
Total Cost	**$ (922,904)**	**$ (2,457,994)**
Reduction in Class 8 Property Tax By Taxing Jurisdiction		
Cities	$ (99,457)	$ (265,111)
Counties	$ (204,604)	$ (545,838)
Consolidated	$ (9,165)	$ (24,394)
Countywide Education	$ (77,053)	$ (205,561)
K-12 Schools	$ (349,298)	$ (929,336)
6-mill	$ (11,610)	$ (30,889)
General Fund	$ (171,716)	$ (456,864)

5) As shown in Table 1, increasing the exemption threshold criteria for taxpayers from $5,000 to $20,000 will *reduce* revenue to the state general fund by $171,716 in FY 2006, and $456,864 in FY 2007: while the 6-mill university account would *decrease* by $11,610 in FY 2006, and $30,889 in FY 2007.
6) In order to effectively administer and ensure compliance with the provisions of this bill, the Department of Revenue would incur annual administrative expenses totaling $18,720 for printing and mailing approximately 40,000 reporting forms.
7) General fund revenue is expected to be reduced by $190,436 ($171,716 + $18,720) in FY 2006, and $475,584 ($456,864 + $18,720) in FY 2007.
8) The university 6-mill account is estimated to decrease by $11,610 in FY 2006, and $20,889 in FY 2007.

Office of Public Instruction

9) The reduction in property tax values from the increase in exemption in class 8 property taxable values would impact the state's obligation to fund the guaranteed tax base aid for school districts and counties.
10) Property tax values decrease by 0.3% in FY 2007. There will be a one-year guaranteed tax base (GTB) cost spike. The guarantee level is determined by the prior year taxable values applied against current year taxable values. The higher guarantee level in FY 2006 will apply to the lower taxable values in FY 2007 and cause increased state contribution as districts levy more mills to compensate for the drop in taxable values.
11) The one-time increased cost will be $127,000 in FY 2007 for district levies as calculated by the school fund model. Countywide retirement GTB will increase $56,000 based on a historical average of 27% of the costs paid for by the state and a FY 2004 county levies equal to $68.6 million (0.3% times $68.6 million local levies times 27%).
12) In FY 2008 and beyond the lower overall level of taxable values will not have a significant impact in statewide guaranteed tax base aid costs.

FISCAL IMPACT:

	FY 2006 Difference	FY 2007 Difference
Expenditures:		
Operating Expenses	$18,720	$18,720
Local Assistance (OPI)	0	183,000
TOTAL	$18,720	$201,720
Funding of Expenditures:		
General Fund (01)	$18,720	$201,720
Revenues:		
General Fund (01)	($171,716)	($456,864)
University System (02)	(11,610)	(30,889)
TOTAL	($183,326)	($487,753)
Net Impact to Fund Balance (Revenue minus Funding of Expenditures):		
General Fund (01)	($190,436)	($658,584)
University System (02)	($11,610)	($30,889)

EFFECT ON COUNTY OR OTHER LOCAL REVENUES OR EXPENDITURES:
If the trigger were met under current law, local governments and schools would likely float mill levies to offset the revenue reductions, property tax burden would then shift to all other property taxpayers. It is estimated that if the trigger was hit in the fall of 2005 and fully implemented by FY 2010, total revenue loss to local governments that would likely be shifted to other taxpayers is approximately $75 million. There would be additional loss attributable to GTB each year of approximately $1,560,000 ($1.1 million + $460,000). See illustration below for a more detailed analysis.

LONG-RANGE IMPACTS:
As shown in Table 2 and 3, the state general fund and university system accounts will see significant savings into the future; again, assuming the trigger would be hit in the fall of 2005. Under SB 284, local governments would not need to increase their mill levies to generate the same amount of revenue had the trigger been met.

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ELIMINATE THE CLASS 8 TRIGGER

a) Revenue estimates in HJR2 do not include any impacts for a class 8 reduction due to the trigger; the fiscal note does not show any fiscal impacts associated with elimination of the trigger.
b) For illustrative purposes, the following analysis shows the impacts if the trigger were met in the fall of 2005. Under current law, the class 8 current 3 percent tax rate would be reduced to 2 percent for tax year 2007; 1 percent for tax year 2008; and 0 percent for tax year 2009 and thereafter.
c) Table 2 illustrates the fiscal impacts over the period FY 2007 through FY 2010 on the state general fund and other taxing jurisdictions if the trigger is hit in the fall of 2005. Most property taxes are paid in the fiscal year following assessment, however some business equipment tax is due in the current fiscal year.

d) Under this proposal, the revenue reductions shown below in Table 2 would not occur, saving the state general fund and other jurisdictions the amount of revenue listed.

Table 2
Fiscal Year - Class 8 Estimated Reduction in Revenue With and Without the Trigger

Fiscal	Estimated Reduction in Property Tax Revenue by Taxing Jurisdiction					
Year	State Government[1]	University 6-Mill[2]	Local Government	Local Schools	TIF	Total
2004	$ -	$ -	$ -	$ -	$ -	$ -
2005	-	-	-	-	-	-
2006	-	-	-	-	-	-
2007	(1,462,047)	(98,026)	(3,659,756)	(2,936,772)	(553,483)	(8,710,083)
2008	(5,402,978)	(361,673)	(14,606,557)	(11,721,035)	(2,125,099)	(34,217,342)
2009	(9,583,721)	(640,530)	(27,981,601)	(22,453,843)	(3,919,802)	(64,579,496)
2010	(12,414,334)	(828,452)	(39,145,839)	(31,412,589)	(5,284,445)	(89,085,659)

[1]State Government amount includes the (average) 1.5 vo-tech mill levy located in five counties
[2]The University 6-Mill is collected on all property, including incremental taxable value.

Additionally, the impacts referred to in the analysis are property tax reductions with respect to the trigger. However, 15-10-420, MCA, allows local governments, to float their mill levies to remain at the prior years revenue level (plus one-half of inflation) and local schools are allowed by provisions of Title 20 to increase mill levies to offset loss in values. Much of the revenue loss could be shifted to other property taxpayers. It is highly likely that local governments would float their mill levies to eliminate some or all of the reduction in property taxes shown above, and effectively shift the property tax burden to other taxpayers. The impacts to the state general fund, the university system, and to tax increment financing districts *would* occur, as these jurisdictions cannot "float" mill levies to counter these impacts.

CLASS 12 RAILROAD AND AIRLINE PROPERTY

e) If the trigger is met, the class 8 business equipment rate reduction would impact the taxable valuation rate applied to class 12 railroad and airline property. As the class 8 tax rate is reduced to 2 percent in tax year 2007; to 1 percent in tax year 2008, and 0 percent in tax year 2009, there would be a commensurate reduction in the class 12 taxable valuation rate, as that rate reflects the composite tax rate of all commercial and industrial property in the state. Table 3 shows the estimated impacts to the class 12 tax rate, holding all else constant, if the trigger is met in the fall of 2005.

Table 3
Property Taxes Paid by Class 12 Property

	FY 2005	FY 2007	FY 2008	FY 2009
Class 8 Tax Rate	3.00%	2.00%	1.00%	0.00%
Class 12 Tax Rate	3.81%	3.56%	3.32%	4.08%
Revenues Assuming Trigger is Met				
State General Fund	4,299,418	4,017,304	3,746,474	4,604,101
University System	270,445	252,699	235,663	289,610
Difference in Revenues - Trigger Not Met				
State General Fund	n.a.	282,114	552,944	(304,683)
University System	n.a.	17,746	34,782	(19,165)

(The tax rate on class 12 property would actually rise again in tax year 2009, as class 8 property would be removed from the calculation of the class 12 tax rate.) Eliminating the trigger will act to prevent any reductions to class 12 taxable value and revenue. Along with the estimated tax rate reduction, Table 3 also shows the estimated impacts to the state general fund and university system accounts from a reduced class 12 tax rate.

Office of Public Instruction – school funding GTB impacts

f) The reduction in property tax values from loss in class 8 property taxable values would impact the state's obligation to fund the guaranteed tax base aid for school districts and counties.

g) Property tax values would decrease by 2.5% in each year FY 2007 through FY 2009. In each other these years there will be a guaranteed tax base (GTB) cost increase from the decline in taxable value. The guarantee level is determined by the prior year taxable values applied against current year taxable values. For example, the higher guarantee level in FY 2006 will apply to the lower taxable values in FY 2007 and cause increased state contribution as districts levy more mills to compensate for the drop in taxable values.

h) The three-year increased cost will be approximately $1.1 million per year for FY 2007 through FY 2009 for district levies as calculated by the school fund model. Countywide retirement GTB will increase $460,000 based on a historical average of 27% of the costs paid for by the state and a FY 2004 county levies equal to $68.6 million (2.5% times $68.6 million local levies times 27%).

i) In FY 2010 and beyond the lower overall level of taxable values will not have a significant impact in statewide guaranteed tax base aid costs.

SUMMARY– CHANGE IN EXEMPTION THRESHOLD AND TRIGGER ILLUSTRATION

j) As shown in Table 1, increasing the exemption threshold criteria for taxpayers from $5,000 to $20,000 will *reduce* revenue to the state general fund by $171,716 in FY 2006, and $456,864 in FY 2007: while the 6-mill university account would *decrease* by $11,610 in FY 2006, and $30,889 in FY 2007.

k) In order to effectively administer and ensure compliance with the provisions of this bill, the Department of Revenue would incur annual administrative expenses totaling $18,720 for printing and mailing approximately 40,000 reporting forms.

l) As Tables 2 and 3 illustrate, eliminating the trigger would *increase* state general fund revenue by $1,744,161 ($1,462,047 + $282,114) in FY2007: while revenues to the university system's 6-mill account would *increase* by $115,772 ($98,026 + 17,746) in FY 2007.

m) General fund costs for costs for schools of approximately $1.56 million per year for three years, FY 2007-FY 2009, would result from reducing property tax rates.

n) Including the impacts if the trigger is met in the fall of 2005, the 6-mill university account would *decrease* by $11,610 in FY 2006, then *increase* by $84,883 ($115,772 - $30,889) in FY 2007.

FISCAL IMPACT IF TRIGGER HIT IN THE FALL OF 2005 (FOR ILLUSTRATION ONLY):

	FY 2006 Difference	FY 2007 Difference
Expenditures:		
Operating Expenses	$18,720	$18,720
Local Assistance – cost to increasing exemption (OPI)	0	183,000
Local Assistance – reduction in cost due to eliminating the trigger (OPI)	0	(1,560,000)
TOTAL	$18,720	($1,358,280)
Funding of Expenditures:		
General Fund (01)	$18,720	($1,358,280)

Revenues:		
General Fund lost revenue due to increasing exemption (01)	($171,716)	($456,864)
General Fund gained due eliminating the trigger (01)	0	1,744,161
University System lost revenue due to increasing exemption (02)	(11,610)	(30,889)
University System gained due eliminating the trigger (02)	0	115,772
TOTAL	($183,326)	$1,829,044
Net Impact to Fund Balance (Revenue minus Funding of Expenditures):		
General Fund (01)	($190,436)	$2,645,577
University System (02)	($11,610)	$84,883